

General Information Letter: Military retirement pay.

August 13, 1998

Dear:

This is in response to your letter dated August 3, 1998 in which you request a letter ruling. The nature of your letter and the information you have provided require that we respond with a General Information Letter (GIL) which is designed to provide general information, is not a statement of Department policy and is not binding on the Department. See 86 Ill. Adm. Code 1200.120(b) and (c), enclosed.

In your letter you have stated the following:

Our Association maintains a file of general information concerning the treatment of military retired pay (and the pay of uniformed personnel of the xxxxxx xxxxxx xxxxxxxx as well as the xxxxxxxx xxxxxxxx and xxxxxxxxxxxxxx xxxxxxxxxxxxxxxx) for income tax purposes be federal, state and local tax authorities. In addition, we publish an annual Income Tax article (1998 edition attached) which is sent to our 400,000 members. In this respect, would you please furnish the information (and excerpts from applicable state tax laws' statutes) indicated in the following questions.

1. Is military retired pay subject to your state income tax regardless of the reason for which a service member was retired? If so, what special exemptions, if any are granted?
2. A person who is retired for military disability (as distinguished from non-disability retirement based on length of service) and has military pay based on percentage of disability must meet the following conditions for federal income tax exemption: (a) On or before September 24, 1995(sic), the member was entitled to receive retired pay computed on the basis of disability, or, (b) On September 24, 1975, he or she was a member of the armed forces (or Reserve component thereof) or under a binding written commitment to become such a member; or, (c) The member receives disability retired pay because of a combat-related injury. The term combat-related injury or sickness means personal injury or sickness incurred as a direct result of armed conflict, or while engaged in extra hazardous service, or under conditions simulating war. (These conditions are codified in 26 U.S. Code, Section 104.) For people covered under a, b, or c above, the tax exemption rules are further clarified as follows: (1) If military retired pay is based on the percentage or degree of disability or is paid under disability retirement laws in effect

before October 1, 1949, the entire amount is exempt from income tax; (2) Where gross military retired pay is based on years of service (2.5 percent for each year), the amount payable solely on percentage of disability is tax exempt. The excess, as reported on Form 1099-R, is taxable income. For persons not covered by the previously specified eligibility criteria - that is, primarily persons who became members of the armed forces after September 24, 1975, and who do not receive disability retired pay because of a combat related injury or who are not eligible for disability compensation administered by the Department of Veterans Affairs - amounts received as disability retired pay are fully subject to taxation. Is any portion of military disability retired pay exempt from state tax, such as on federal returns? If so, what specific exemptions, if any, are granted?

3. What is the address and telephone number service members can use to obtain more detailed information and order tax forms?
4. What is your web site address?
5. Do you allow taxpayers to file (a) forms generated by computerized tax programs or (b) file electronically by modem?
6. Does your state use the Kansas/California method for taxing nonresidents - ascertaining what the member's tax rate would have been if all of his or her income has been taxable in the state and taxing the taxable portion at that rate?
7. Does your state permit separate returns even if a joint federal return is filed?

Previous information we have received from your state is reflected in the attached article under the heading "State Income Tax Information on Military Retired Pay." The purpose of this correspondence is to validate or update your state's data as contained therein.

#### RULING

Under the Illinois Income Tax Act ("the IITA"; 35 ILCS 5/101 et seq.) an individual's Illinois net income is determined by starting with the amount of his or her federal adjusted gross income (AGI), then modifying that amount in accordance with specific statutory addition and subtraction provisions. (See IITA §202 and §203). Thus, amounts not included in an individual's federal AGI, unless the subject of a statutory addition provision, are not subject to Illinois income tax. On the other hand, amounts included in a taxpayer's federal AGI are not subject to Illinois income tax if there is an applicable statutory subtraction provision. The IITA contains no addition provision relating to amounts received as distributions from any retirement or disability plan for employees of any governmental agency or unit.

At the same time IITA section 203(a)(2)(F) provides the following subtraction provision:

An amount equal to all amounts included in [federal AGI]...as distributions under the provisions of any retirement or disability plan for employees of any governmental agency or unit.

Illinois Income Tax Regulations extend to the term "employee" the same meaning as under Internal Revenue Code (IRC) section 3401(c) and Treasury Regulation 31.3401(c)-1 (86 Ill. Adm. Code 100.3100(b)). Section 3401(c) provides that the term employee includes an employee of the United States or any agency or instrumentality thereof. Thus, the term employee for purposes of the IITA includes a member of the United States Armed Forces.

Accordingly, regarding the first question posed in your letter, any amount received as military retired pay pursuant to a retirement plan for members of the U.S. Armed Forces is not subject to Illinois income tax, regardless of the reason for which the service member was retired. Likewise, regarding your second question, any amount received as military disability retired pay pursuant to a disability plan for members of the U.S. Armed Forces is not subject to Illinois income tax.

Regarding your third question, the address and telephone number service members can use to obtain more detailed information appear below:

Illinois Department of Revenue  
Willard Ice Building  
101 West Jefferson Street  
P.O. Box 19044  
Springfield, Illinois 62794-9044  
Telephone:  
1 800-732-8866,  
1 217-782-3336,  
TDD at 1 800-544-5304

The address and telephone number service members can use to order tax forms appear below:

Illinois Department of Revenue  
P.O. Box 19010  
Springfield, Illinois 62794-9010  
Telephone: 1 800-356-6302

Regarding your fourth question, the Department's Web site address is <[www.revenue.state.il.us](http://www.revenue.state.il.us)>.

Regarding your fifth question, computer-generated forms may be filed provided the Department has approved such forms. Form approval for software companies that provide computer-generated forms is given at the company level.

In addition, electronic filing of Illinois income tax returns is permitted for certain individuals pursuant to Regulations found at 86 Ill Adm. Code 105/100 et seq. (copy enclosed).

Regarding your sixth question, IITA section 201(b)(3) provides that the entire Illinois net income of an individual, including a nonresident individual, be taxed at a flat rate of 3 percent. The Kansas/California method you refer to is therefore irrelevant to the determination of Illinois income tax.

Regarding your seventh question, IITA section 502(c)(2) requires, with one exception, that spouses filing a joint federal income tax return file a joint Illinois income tax return. The one exception is found at IITA section 502(c)(3). That section mandates the filing of separate Illinois income tax returns by spouses where only one of the spouses is a resident, unless such

spouses file an election to determine their joint net income and file a joint return as if both were residents.

As stated above, this is a GIL that does not constitute a statement of policy that applies, interprets or prescribes the tax laws, and it is not binding on the Department. If you are not under audit and you wish to obtain a Private letter Ruling regarding your factual situation, please submit all of the information set out in items 1 through 8 of the enclosed copy of section 1200.110(b).

Sincerely,

Brian L. Stocker  
Staff Attorney - Income Tax